Trade Stocks™

SECRETS TO FIND WINNING PENNY STOCKS

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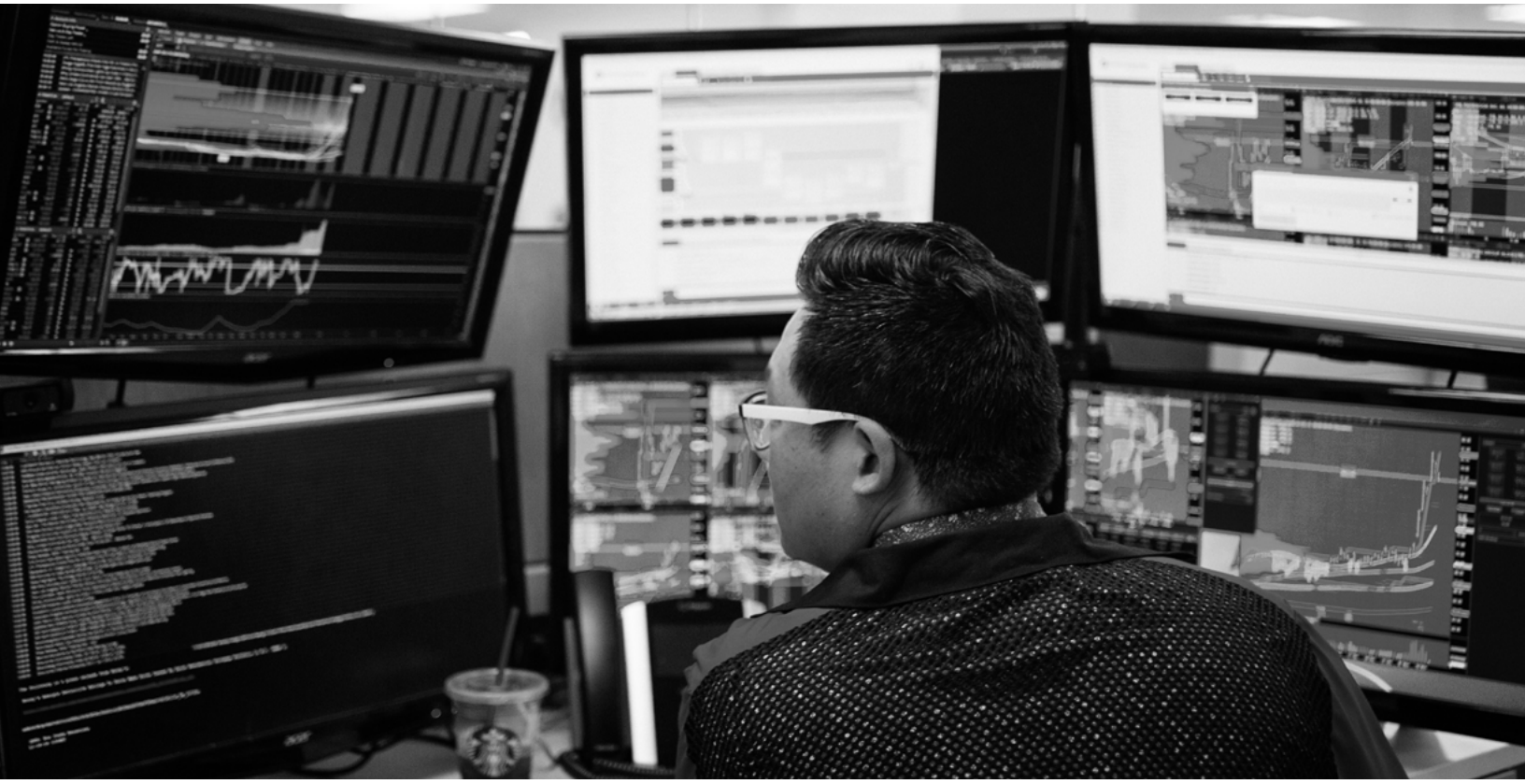
ABOUT THE AUTHOR



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Charles Moon is a technical-analysis based trader whose experience lies in active portfolio management. A patient educator, Charles excels at one-on-one mentoring and can make complex concepts sound simple. Prior to joining the ranks of Prosper Trading Academy, Charles was a proprietary equities trader with Great Point Capital LLC.

Introduction To Trading Penny Stocks

The stock markets are generally the most desirable assets to trade and invest in. You invest your money and essentially pray for positive yields over years on end. There are dividend plays, longer term holdings in big cap names and then there are those that want to hit a home run on a stock. That is where penny stocks come into the picture. Truth is, we see a massive response in some names that are usually tied with the technology or pharmaceutical sectors. It is a chance to get in a ground zero and leverage your money. Essentially, these smaller caps are highly desired for volatility and opportunity. For those that trade with smaller account sizes, this might be the best way to truly leverage your position with the aim of hitting that home run.

Why Penny Stocks?

It is pretty simple if you think about it. People like action and opportunity but they also love to dream. Have you ever sat there and dreamed about winning a huge lottery jackpot? That is kind of the grandeur people will think about when taking on 10,000 shares of a stock worth a few pennies. Maybe only taking on

a few thousand of a biotech stock worth a couple of dollars in hope their phase 3 trial will pass. Maybe a massive buyout from companies like Amazon, Google, Microsoft and Facebook can happen. Frankly, it is a bit like buying a lottery ticket. Monster Beverage (MNST) is a name that comes to mind as a penny stock success story. MNST was literally a penny stock as their shares were once worth $0.01 and has hit an all time high of $67.24 (at the time of this writing). However, this isn't typical regarding penny stocks. More than anything, they should be viewed more as trading products versus investable assets.

Trading vs. Investing

Should you trade or should you invest? That is the question you must ask yourself here. In regards to penny stocks, trading is really how you can capitalize on the volatile moves these stocks can make. If you were to invest in these names, you may get the move you were anticipating, but most likely wouldn't make a move in regards to the management of the trade. Buy for yield and hold for growth. The problem with that is these stocks tend to "pop and drop". That means the stock may jump for a huge

percentage gain and then retraces back to where it started in a very short period. As a trader, you would be prepared to act if the stock makes this move. You would have a plan in place and be able to react in accordance. As an Investor, you would hold through that move and you may not see any yield as a result. Additionally, you tie up your money and could possibly miss out on the next opportunity.

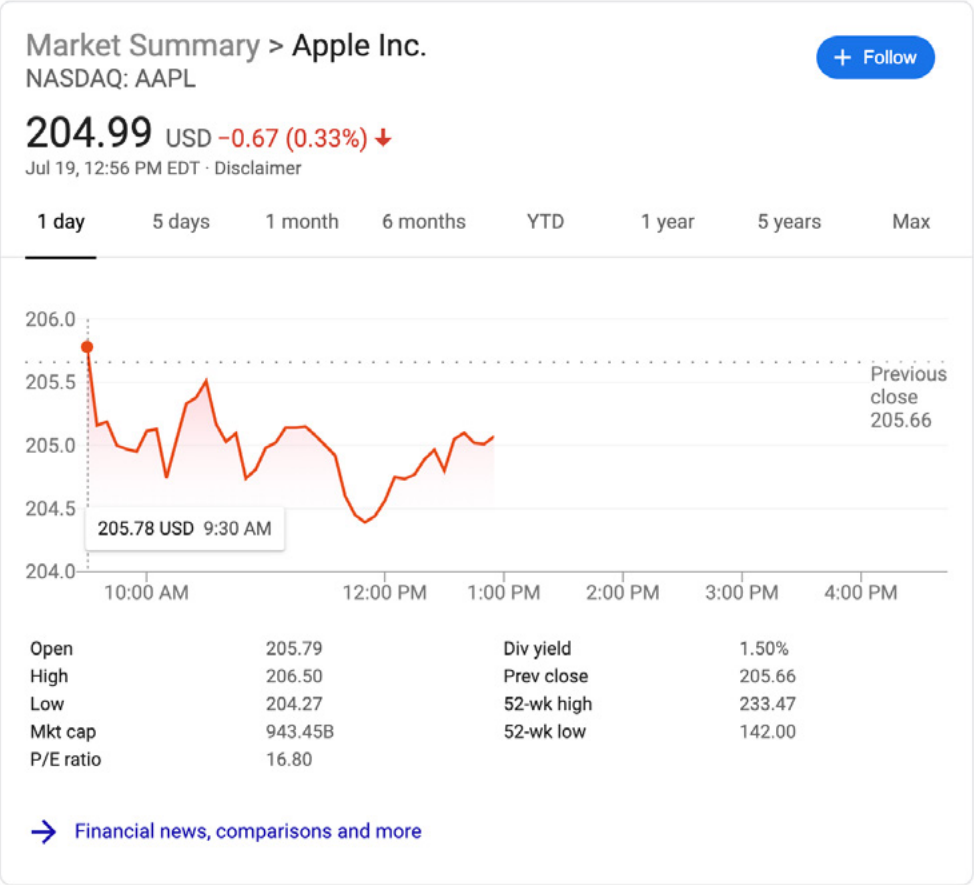
What is an Over-the-Counter (OTC) Or Pink Sheet Stock?

Generally speaking, it means you are trading an equity that is not listed on a major exchange. They are not subjected to the same regulatory rules as listed stocks and these stocks are usually speculative companies or foreign based equites. While some foreign based companies (Nintendo comes to mind) will trade OTC instead of spending millions of dollars to stay compliant.

Some stocks that trade OTC were stocks that got delisted due to lack of financial disclosure. Others trade OTC after being kicked off the exchange due to low stock price. Whatever the reason maybe, there is some additional risk associated with these stocks due to the lack of liquidity and institutional interest.

Why Trade Penny Stocks?

There are plenty of reasons to consider trading penny stocks. The biggest reason for me is leverage if you trade with a smaller account size. Imagine trying to trade AAPL or AMZN with a



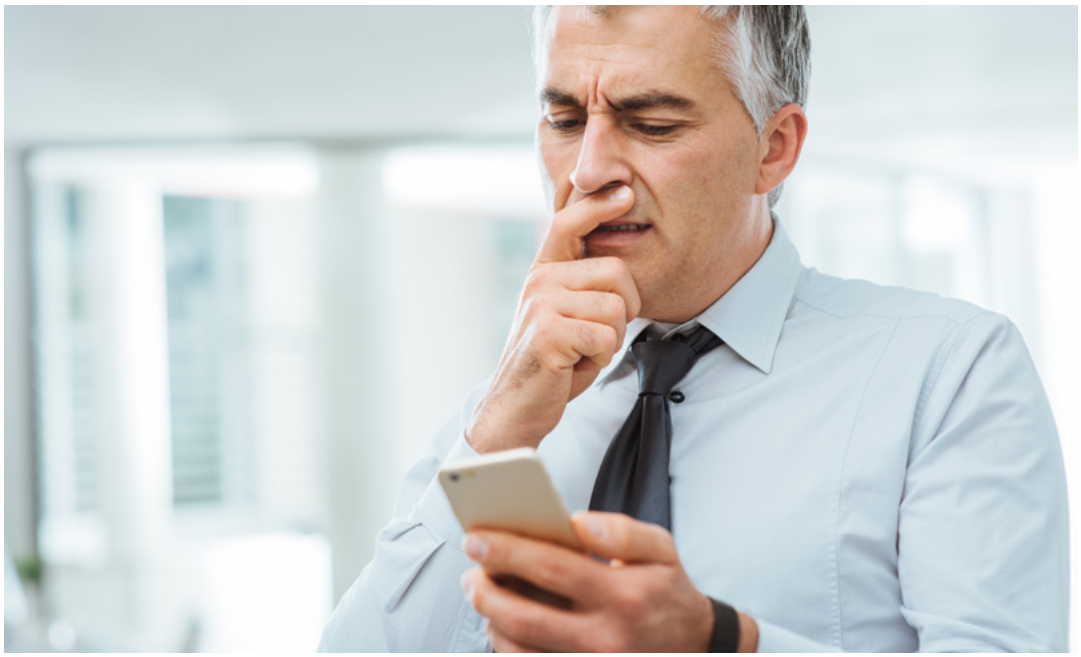
$10,000 account. Even if you traded with options in these names, you could still not allocate enough contracts to make things worth your time. Add to that the risk associated with these names, dealing with the complexity of options trading and

factoring in time decay can complicate the trades. Penny stocks offer the ability to take on a large share size and capitalize on smaller moves. If you consider the downside risk is much smaller than the larger names, that helps you with your risk management. If a penny stock is worth $1.00 then the most you can lose is $1.00 per share.

Obviously, you wouldn't want to hold the position until the stock goes to $0.00 if you were in the trade. However, that is a reality you have to face in any stock although it would take an Enron type of scandal for that to happen. The fact that your risk is limited allows you to leverage positions to a much greater extent than the large cap names. You also have a greater chance of larger profits on smaller moves. If AAPL trades at $170.00 and if stock "ABCD" (just an example of a penny stock) trades at $1.70, you can trade many more shares in ABCD than AAPL. Also, imagine both stocks move $0.50 in your favor if you took a trade. The profits in ABCD will be much larger (100x) than it would be if you held shares in AAPL instead. On a $10,000 account, you can trade over 5,000 shares if you maxed out your buying power in stock ABCD. If you traded AAPL that would only equate to 58 shares MAX. That $0.50 profit on 58 shares = $29.00 before transaction fees. However, with stock ABCD, that profit total would = $2,900 before transaction fees. Let that sink in for a moment. Yes, it is exciting to tell your friends and family that you trade AAPL, but does that matter to you when you see the difference in profit potential? Imagine what kind of leverage you can have with a larger size account. That also applies to smaller account sizes. Imagine being able to grab these types of profits in a shorter term time frame instead of hoping the stock will one day garner yield.

The Risk Associated With Trading

I hate to say this, but trading is not for everyone. Can anyone learn how to trade? The resounding answer to that is YES! I work with clients from all backgrounds that have learned to trade. The key factor is risk management and discipline. If you do not possess these traits within your trading plan, the likelihood of success is low to say the least. Taking losses are just a part of the game and comes with the territory. Think of these losses as a price to do business. Stubborn thinking and trying to outsmart the markets generally leads to large losses. These large drawdowns are devastating to a small trading account. That is



why it's imperative to be disciplined. You must exit when the max designated drawdown limit is hit. To ignore, hope or think a stock could rally back to save your tail is wishful thinking. Some stocks just never recover from their losses. Sometimes the

stock will recover but it takes years to rally back. Imagine tying up your money in a terrible trade for years and then it finally recovers to your breakeven price. It's a bit of a double whammy. The stock made the move and you bought in late. Then you're stuck and you missed out on the subsequent rally that gets you to breakeven. That is on top of the thousands of missed trades in other stock names because you had no available cash. That is also the best case scenario for the trader that is stuck in the trade. What if the stock never recovers? You not only wasted time tying up your money, but you still have to take the substantial loss on top of that. With the proper information and proper trading system coupled with the risk management and discipline, it could lead you down a path of success. However, without all of the above, you could just end up losing most, if not all, of your cash. If you are going to actively pursue risk which is the stock market, then you should care about what happens to your cash. Of course, no one plays the markets wanting to lose their money. Unfortunately, that is the outcome for those that do not care enough about their money. Do not end up as one of these people! Give a damn about your money!

The Holy Grail of Indicators

Now that I have your attention, I just want to state something.... THERE IS NO SUCH THING AS the Holy Grail Of Indicators! I will say that money is king. That is where your attention has to be from now on after reading this. Money will always be king regarding the markets. If an order worth $15 billion tries to buy in a stock and at the same time, $20 billion tries to sell, that $20 billion will ALWAYS win that battle and that war. If you want to focus on indicators, I would suggest focusing on volume based indicators and scanners. I want to see big volume and align myself with them. To state another way, I am looking to join the momentum instead of going against it. Think of being a mile or two offshore in the ocean. Regardless if you are a strong swimmer or not, you are more likely to survive if you swim WITH instead of AGAINST the current. Sorry for the caps but I cannot pound on this point enough. Join the big volume instead of going against it. It will be the easiest way to profits in one sided trading. It could be as simple as watching "time and sales" or you can place volume based indicators on your trading platform that can alert you in real time if something comes up. The same goes for scanners where you can specifically scan for large volume introduced into a stock.

There are a variety of ways to decipher all of this information but you must discover what works best for you. I will say that volume has to play a role one way or the other. I find that success is more more consistent when you associate your speculation with larger than normal volume. Usually when big money talks out loud, you should be more than willing to listen.

Problems Most Penny Stock Traders Face

Here is the biggest issue for penny stock traders. They do not know what to trade. You can have a massive watchlist with thousands of names and struggle to see anything worth trading on a daily basis. Those same names may remain dormant for months if not years. Then they can move and leave you behind because your focus was on other names in your list. Trying to focus on thousands of names daily is just too much even for the most seasoned of traders. Imagine having actual trades in a lot of these names and trying to manage them all on top of just trying to analyze which stock you should be trading. It is damn near impossible to do and frankly will be a losing strategy. I concentrate on a very small list on a daily basis. My watchlist may be completely different the following day. I do not want to hold these positions overnight. My focus is solely concentrated on short bursts in low priced names and those bursts must be due to larger than normal volume. That is why I use a scanner...

The Power of a Scanner

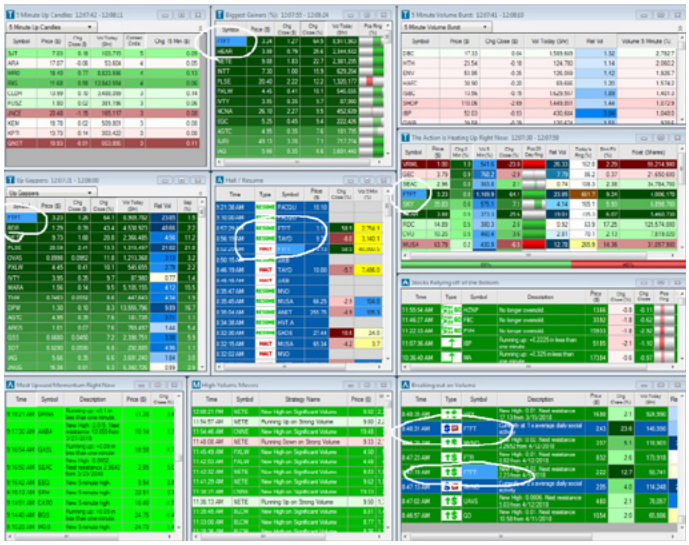
To search for penny names on a daily basis, you can create a watchlist that is a mile long and struggle to find the ones that are moving. By moving, I mean substantial percentage gains. To see the move after the fact accomplishes nothing for the trader. A scanner can pinpoint these moves right when it happens. In some instances, we can find these names just BEFORE the move is made. It will depend on the filter settings and the design of the scanner. I am there to teach you how to maximize a tool like our scanner to reveal only the best trading opportunities. As short term traders, these high percentage moves are all we want to look for. When buy or sell volume is introduced in a significant and aggressive manner, it can cause a huge shift in stock price. The ideal stock I am looking for are low-float names that move on volume. A “low float” stock is one with a relatively low number of shares available for trading. Stocks with a low float and low market-cap tend to be volatile, and can make huge moves to the upside very quickly if they have a positive catalyst. While large volume can shift a stock like AAPL by $0.10 - $0.20 right away, that same amount of money can shift a $3.00 stock to $6.00 very quickly. That is why we must find these stocks just before or right when the move starts to happen. Otherwise, you will be left in the dust. People can pay as little as a few hundred dollars a year for a very basic scanner or pay tens of thousands of dollars to get the top of the line models. Prosper Trading Academy provides our clients with a scanner broadcast in the signal room everyday. Once our clients get proficient with our scanner, they have limitless opportunities daily to catch that diamond in the rough.

This is a layout of my trading room. This is exactly what you will see when you log in with me in the morning.

How I Prepare to Trade

Before the stock market's opening bell, I will look over my scanner before I get started. I am focusing on three different scanners. My "Up Gapper" which will show me stock names that are up premarket based on volume and percentage from the previous day's closing price. My "Heating Up Right Now" scan

will also highlight any up trending names and expansion beyond recent 1 min trading ranges. Lastly I will look at my "Breaking Out on Volume" scanner to verify either high volume moves or trending ticker symbols on social media. Social media mentions are important to the sentiment gauge of these names. Since penny stocks are rarely if ever traded by institutional money. Since these penny stocks are mainly retail traders duking it out for profits, it is always a good idea to know the current sentiment of the stock. Let's take a look at how I approach trading opportunities...



1. You can see on the Scanner that FTFT was on several of my scans…

2. Once I pull up the stock on my platform, I look to see if I have the proper buy signals. Once signal is valid, I jump into the signal and upon entry I will also place my stop loss order.

3. As you can see on the chart, the stock moved with strength until it was halted due to a circuit breaker trigger. Stop is trailed up prior to halt based on the methodology.

You must decide which route you want to go if you decide to pursue trading. The ability to build quickly and leverage your positions is clearly with penny stocks. The risk can be significant since these stocks are essentially unregulated. Unless you plan on holding for a long period of time in these names, your exposure to the markets is short term and limited. For those trying to build a small account into a larger one which will allow them to be able to trade large cap names, this might be the best path to take at first. If you decide to educate yourself and develop the skills need to succeed, then don't wait any longer to reach out to us. I look forward to seeing you in the classroom!